

# **MINUTES OF THE CAPITAL PROJECTS AND BOND OVERSIGHT COMMITTEE**

**June 16, 1998**

The Capital Projects and Bond Oversight Committee met on Tuesday, June 16, 1998, at 1:00 PM, in Room 129 of the Capitol Annex. Representative Robert Damron, Chair, called the meeting to order, and the secretary called the roll.

Present were:

Members: Representative Robert Damron, Chairman; Senator Robert Leeper, Vice Chairman; Senators Tom Buford and Denny Nunnolley; Representatives Drew Graham, Paul Marcotte, and Jim Wayne.

Guests: Roger Burge, Allen Holt, Paula Moore-Carson, Ron Carson, and Bill Hintze, Governor's Office for Policy and Management; Paris Hopkins, Governor's Office; Merl Hackbart, Senior Policy Advisor to the Governor on Budget and Policy Issues; Commissioner Armond Russ and Jim Abbott, Department for Facilities Management; Marilyn Eaton-Thomas, Bart Hardin, and Tom Howard, Office of Financial Management and Economic Analysis; Mayor Dennis Deibel, City of Crestwood; Holly Nicholas, PDR Engineers; Bill Gatewood and Kay Hines, Division of Water; Jerry Tuggle and Jim Sanders, Western Kentucky University; Bob Bender, Department of Parks; Bob Carter, Military Affairs; John McNulty, Lt. Governor's Office; C. Bunch, Department of Corrections; Debbie McGuffey, Council on Postsecondary Education; Sally Hamilton and Doris Holtzclaw, Kentucky Educational Television; Roy Strange, Associated Industries of Kentucky; Kevin Mason, Workforce Development Cabinet; James Everett, Kentucky Council of Area Development Districts; Dr. Robert Tarvin, School Facilities Construction Commission; Mary Allen, University of Kentucky; Kim Burch and Charles Shirley, LRC.

LRC Staff: Mary Lynn Collins, Pat Ingram, Lou Pierce, Jack Affeldt, and Shawn Bowen.

Chairman Damron reviewed correspondence items in members' folders which included the Kentucky Lottery Corporation's monthly financial status report for April 1998 and correspondence from Dr. William Martin, Chair of the Kentucky Heritage Land Conservation Fund Board.

Chairman Damron noted that at its the May meeting, the Committee passed over a Kentucky Infrastructure Authority (KIA) Wastewater loan for the city of Crestwood. A loan in the amount of \$5,956,634 was requested by Crestwood to construct a sewer system. During the Committee's review, several members questioned the project's engineering fees, but no one from the city of Crestwood was available to answer questions relating to the project. He said the Committee delayed action until the June meeting in order to hear from Crestwood city officials. However, shortly after the May meeting Secretary McCarty notified the Chair that the city of Crestwood was unable to hold project bids until the Committee's June meeting and consequently, he had authorized KIA staff to proceed with the loan. Chairman Damron said when he received notice from Secretary McCarty, he corresponded with other Committee members, and determined there was still considerable interest in reviewing the Crestwood loan. Consequently, Dennis Deibel, the Mayor of Crestwood, was invited to the meeting.

Chairman Damron introduced Mayor Deibel; Marilyn Eaton-Thomas, KIA; Holly Nicholas, PDR Engineers; and Bill Gatewood, Division of Water (DOW).

Mayor Deibel thanked the Committee for inviting him to discuss the project's engineering fees. He began by explaining that Crestwood was in a situation last month where the loss of the project bid could have cost the project an additional \$750,000-\$1,000,000.

Mayor Deibel said this project began 25 years ago, starting with the Oldham County Water District, and Crestwood took it over about 10 years ago. The mayor, noting he serves on a voluntary basis, said the city of Crestwood has no paid staff and the city relied on PDR Engineers to accomplish tasks normally handled by city employees. Mayor Deibel said PDR Engineers prepared two interlocal agreements: one was with Oldham County, Jefferson County, and Crestwood for a regionalizational project with the Louisville-Jefferson County Metropolitan Sewer District (MSD), and another agreement was formalized between the cities of Park Lake and Crestwood. Mayor Deibel said PDR Engineers subcontracted with another firm to acquire over 100 easements for the construction of this project at a cost of \$525 per easement,

Mayor Deibel said city officials knew up front what the engineering fees would be, and felt the fees to be affordable, and to delay the project would have been more costly.

Mayor Deibel said the KIA Board raised the same questions about engineering fees as the Committee, but approval was granted after he explained the situation to Board members. Mayor Deibel said he was not aware of the Committee's role; otherwise, he would have been available last month to explain Crestwood's position.

Representative Wayne said the Committee's intention was not to delay the project or to put the city in a position where the project would cost them more money. However, the Committee felt it needed more information. In response to a question from Representative Wayne, Ms. Eaton-Thomas said project bids for the Wastewater Revolving Loan Program have to be in place before a project can be presented to the KIA Board for approval. She added there is a 90-day window for the KIA Board to approve the project and for the Committee to review it before it goes to construction. Representative Wayne said this process puts a time constraint on the Committee, and once projects are presented to the Committee, there is a limited amount of time to review those projects. Ms. Eaton-Thomas said hopefully in the future, KIA can time projects better so Committee members will have more time to review them. Representative Wayne said he hoped things will work smoother in the future because limited time to review projects puts the Committee in a bind when it is trying to do its job – representing the interest of the Commonwealth.

Representative Wayne asked why both resident inspections and on-site inspections are needed for this project. Mr. Bill Gatewood, DOW, said the resident inspections are normally provided by a non-engineering inspector who is frequently on the construction site. Most of the inspection costs for the Crestwood project, \$333,083, are for resident inspectors. He said a small amount of money, approximately \$6,000, is being used for on-site inspection, which is performed by the engineer who is the project manager. Ms. Eaton-Thomas added that both resident and on-site inspections are typically included in wastewater projects.

In response to another question from Representative Wayne, Ms. Eaton-Thomas said KIA is not adhering to the Rural Development (RD) fee schedule for this loan because it is partially EPA funded; instead, they rely on the DOW to review costs. Mr. Gatewood explained that the DOW takes a totally different approach to evaluating

Representative Wayne asked if the RD schedule will be used for new drinking water programs. Ms. Eaton-Thomas responded that although the final decision has not been made, they probably will use the RD schedule for the new drinking water program.

In response to a question from Representative Wayne, Mayor Deibel said he thought PDR's pricing was in line for the work involved. Representative Wayne said since 1995, the Committee has reviewed six different KIA Fund A loans that exceeded \$1 million, and none had engineering fees as high as Crestwood's. Mayor Deibel said if he had hired a city employee to take care of the things PDR did, the person would have had to be extremely knowledgeable about sewer systems, MSD, and Jefferson and Oldham County Governments. He added if he had hired a city employee, it is probable the project could have been completed at a lower cost, but without the expertise PDR was able to provide. Ms. Holly Nicholas, PDR Engineers, said during design, subdivisions not included in the original project design decided to be part of the project, which caused PDR to resurvey and redesign portions of the project.

Ms. Nicholas said this project was bid as four separate contracts in hopes of getting better bids, and she reported they received very good bids. She added if they had adhered to the RD fee schedule, there would have been only one inspector and one contract instead of four resident inspectors and four contracts.

Mayor Deibel said once the design phase was 80% complete, additional subdivisions and businesses requested inclusion in the sewer project. He said PDR acquired additional easements, and twice redesigned the project to include the additional subdivisions and businesses.

Chairman Damron noted that one problem was the mayor was not made aware of the Committee's role in the process. He asked Ms. Eaton-Thomas if KIA informed local governments of the Committee's role in processing KIA loan requests. Ms. Eaton-Thomas responded that KIA does not inform local governments of the Committee's role in the decision-making process. He said KIA, in the future, should inform prospective loan recipients that the Committee's review is part of the loan approval process. He said had the mayor been made aware of the Committee's review, he would have been available at last month's meeting to answer questions, and Secretary McCarty would not have been put in the position of having to preempt the Committee's review process.

once the top-ranked firm is selected, its price can either be accepted or declined, and if it is declined, the contracting agency begins negotiations with the second-ranked firm. Ms. Eaton-Thomas said if the Committee needs to be involved in the decisions regarding procurement and engineering fees, it may need to be more involved in the earlier stages of the process.

In response to a question from Representative Marcotte, Mayor Deibel responded that Crestwood has been working with the DOW for three or four years. Even before submitting applications, they sought DOW's support for the regional concept of utilizing MSD of Louisville.

Chairman Damron asked if local governments have the option to bid engineering fees. Ms. Eaton-Thomas and Mr. Gatewood agreed they do not have the option under KIA funding. In response to another question from Chairman Damron, Mr. Gatewood said rather than adhering to a fee schedule, the applicant submits a breakdown of the kind of employees to be used on the project and the hourly pay rates. DOW engineers then review this information to see if it's reasonable for the type of project. Mr. Gatewood said the DOW did not approve the entire engineering fee for the Crestwood project. They approved the fees associated with planning, design, and construction. They did not approve as part of the KIA loan the engineering fees for other services.

Chairman Damron asked Mr. Gatewood if he thought local governments should have the option of competitive bidding. Mr. Gatewood responded that he thought the qualification-based procedure has worked well, and he did not see a problem with the current procedure. Chairman Damron asked if the loan procedures discussed today apply to other projects or just to wastewater projects. Ms. Eaton-Thomas said this is the normal procurement procedure for almost any kind of agency that funds local projects. The difference in the KIA Fund A loan program and other KIA programs is not the procurement of architects and engineers but the way fees are set. Fund A uses a DOW review, and the other KIA programs use a fee schedule. Ms. Nicholas said although it doesn't happen very often, her firm has participated in competitive bidding in some federally-funded programs.

Chairman Damron asked if the current method for procuring engineering contracts for local governments is the most effective. Mayor Deibel responded that local authorities have enough knowledge to know if they are being overcharged. He added that local governments already have the ability to either accept or decline a bid.

Senator Buford asked what the initial estimate was for engineering fees before PDR found out they would have to provide additional services to Crestwood. Mayor Deibel said the city anticipated from the beginning the need for the extra engineering fees. They knew they would need an engineering firm to work on the project that was familiar with MSD and that could prepare the necessary interlocal agreements.

In response to a question from Senator Buford, Ms. Nicholas said a lot of local governments have the staff to handle easement acquisitions, but PDR always prepares the deed descriptions for the easement forms and provides geotechnical services. She added that the contracting firm typically writes the Operations and Management Manual required by the DOW, and archaeological services have to be provided by a licensed archaeologist. Ms. Nicholas said PDR normally does not prepare interlocal agreements or conduct assessments.

In response to another question from Senator Buford, Ms. Nicholas said the county Property Valuation Administration (PVA) office did not help with conducting assessments.

Chairman Damron said since Secretary McCarty has already approved the KIA Fund A loan for the city of Crestwood, no action from the Committee is necessary.

Next, Chairman Damron called on Mr. Jim Abbott, Director, Division of Real Properties, to discuss state lease renewals with annual costs over \$200,000. Chairman Damron noted that in addition to the four lease renewals submitted for the June meeting, six lease renewals were submitted for the July meeting. He said since the lease renewals were so similar and also located in Franklin County, he thought it was important to look at all the leases at the same time. He said the six additional lease renewals were added to the agenda at his request.

Chairman Damron noted that ads were placed in newspapers for each of the ten lease renewals, and in each case, the only respondent was the current landlord. He said this reinforces certain findings of a study done last year by Fantus Consulting for the Finance and Administration Cabinet – that there is a lack of available office space for lease in Frankfort.

Mr. Abbott said of the 11 lease contracts, with annual costs exceeding \$200,000 and with expiration dates of 6/30/98, one contract was renewed with the same terms

because the longer the lease contract, the longer the lessor forgoes the opportunity to ask for additional increases.

Mr. Abbott said the overall increase in the ten contracts being presented today represent approximately a 2.5% annualized rate increase with a duration of those contracts ranging from three to four years. He said on most of the lease renewal contracts, the contracts include leasehold improvements requested by the user agency. He also noted the Consumer Price Index for that same period is projected to be 3.107%.

The leases approved included three properties for the Natural Resources and Environmental Protection Cabinet: PR-2615, located in Fort Boone Plaza; PR-3322, located at Hudson Hollow; and PR-3835, located at 803 Schenkel Lane; the Revenue Cabinet (PR-3747 and PR-3882), for property located at 100 and 200 Fair Oaks Lane; the Cabinet for Health Services (PR-3734), for property located at 200 Fair Oaks Lane, Building No. 2; the Office of the Attorney General (PR-3799), for property located at 1024 Capital Center Drive; the Labor Cabinet (PR-1069), for property located on US 127 South; the Cabinet for Families and Children (PR-3590), for property located on Athletic Drive; and the Kentucky Higher Education Assistance Authority (PR-3748), for property located on US 127 South. The total annual increase of the 10 lease renewals is \$456,876.

In response to a question from Chairman Damron, Mr. Abbott said the cost of the leasehold renovations is not covered under the prevailing wage law. Chairman Damron said according to the Labor Cabinet, the prevailing wage law applies to built-to-suit construction. He asked Mr. Abbott if the Division of Real Properties has reviewed the statute regarding prevailing wage and how it relates to rental property for state use. Mr. Abbott said they have not been faced with that dilemma and none of the leasehold improvements included in the leases before the Committee today are in excess of the prevailing wage threshold of \$250,000. Chairman Damron suggested Mr. Abbott review the prevailing wage matter and consider how it applies to leased property.

Chairman Damron said currently leases with an annual cost in excess of \$200,000 must be approved by the Committee and, pursuant to House bill 704 which goes into effect next month, leases with an annual cost in excess of \$100,000 will also be reviewed by the Committee.

was withdrawn. Mr. Abbott added that Real Properties is continuing to work with KCTCS to evaluate its space needs.

Chairman Damron then called on Mr. Bill Hintze, Deputy State Budget Director, Governor's Office for Policy and Management (GOPM), and Commissioner Armond Russ, Department for Facilities Management, to report on three projects submitted by the Finance and Administration Cabinet.

Mr. Hintze said the Wendell H. Ford Regional Training Site project in Muhlenberg County has been under development for several years. He said this project was authorized for \$4,502,000, and is 100% federally funded. Mr. Hintze reported the federal government is willing to support a scope increase in the amount of \$1,742,140, which will be used to address cost overruns because of earlier delays in federal funds. The revised project would be \$6,244,140.

Representative Wayne asked how many training centers are located throughout the state. Mr. Hintze responded there are two large ones, and Mr. Bob Carter, Director of Facilities, Department of Military Affairs, added the other training facility, located in Barbourville, is a federal lease while the Wendell H. Ford Training Center is on state-owned property. In response to a question from Representative Wayne, Mr. Carter said the number of people trained in these facilities each year is increasing. He said the facilities are used to train 6,000 soldiers in the National Guard, as well as those in active duty at Fort Campbell and Fort Knox.

Chairman Damron said it is important to note this project is 100% federally funded, and if the federal government does not come through with the appropriation, the project will be scaled back.

Representative Marcotte made a motion to approve the federally-funded scope increase for the Wendell H. Ford Regional Training Center project. The motion was seconded by Senator Buford and passed by voice vote.

Next, Mr. Hintze discussed a project for Kentucky Educational Television that involved the purchase and installation of three digital uplinks at Eastern Kentucky University, Murray State University, and the University of Louisville. He said this project was originally funded by a grant from the National Telecommunications and Information Administration (NTIA) for \$610,028. Mr. Hintze said bids for the project came in over



Senator Buford made a motion to approve the cost overrun for the KET digital uplink project. The motion was seconded by Representative Marcotte and passed by voice vote.

The last Finance project Mr. Hintze discussed was a life safety project for Western Kentucky University (WKU) that involved the replacement of a fume hood. He said these projects can sometimes takes years to phase in and scope increases are not uncommon with this type of project. He said the project was originally authorized for \$3,125,000 by the 1996 General Assembly (\$2,260,000 in General Funds and \$865,000 in restricted agency funds). He reported a scope increase of \$468,000 (15%) is now necessary to complete work on the project. Mr. Hintze said the source of funds for the cost overrun will be uncommitted balances from surplus funds in WKU's life safety bond clearing accounts. The revised scope for the project would be \$3,593,000.

Chairman Damron noted the scope increase for the WKU project is not being funded from the Capital Construction and Equipment Purchase Contingency Account. Mr. Hintze explained the policy of both the Finance Cabinet and GOPM is to use the contingency account only as a last resort for funding cost overruns.

Senator Buford made a motion to approve the cost overrun on the WKU fume hood replacement project. The motion was seconded by Senator Leeper and passed by voice vote.

Chairman Damron called on Mr. Tom Howard, Office of Financial Management and Economic Analysis (OFMEA), to discuss bond activity reports. Mr. Tom Howard discussed a project report for Kentucky Asset/Liability Commission (KALC) Project Notes, 1998 Agency Fund Series. He said this is a new program being developed by KALC to provide short-term financing for agency-funded line item and pool projects. Mr. Howard said state universities will benefit from this program because they will not have to use as much of their own internal resources to fund construction projects until they are reimbursed from bond proceeds. He said universities can borrow money in the short-term tax-exempt commercial paper or money market at 3.5-4% range and continue to invest their own funds at taxable rates of return in the range of 5.5%-6%. He said \$100,000,000 in KALC Project Notes have been authorized, to be used for the following projects: Morehead State University Wellness Facility; UK Center for Rural Health; ECU Law Enforcement Training Center; UK Commonwealth Stadium Expansion; KY Higher Ed. Assistance Authority Bldg.; KY River Water Release System;

Senator Nunnelley made the motion to approve KALC Project Notes, 1998 Agency Fund Series. The motion was seconded by Representative Wayne and passed by voice vote.

Next, Mr. Howard discussed KALC General Fund Tax and Revenue Anticipation Notes (TRANS), 1998 Series A. He noted the information being provided is a preliminary estimate for the upcoming year. Mr. Howard said KALC expects to authorize approximately \$400,000,000 in TRANS, to be used to manage cash flows of the General Fund. Mr. Howard said the initial issuance (\$200,000,000) will be sold soon, and will begin earning arbitrage on the first available day. Mr. Howard said before committing to any additional borrowings, the KALC will wait to see how the money flows out of the Surplus Expenditure Plan. The expected gross proceeds are \$401,000,000 for 364 days at 4%. Peck Shaffer & Williams will serve as bond counsel; Salomon Smith Barney as underwriter; and OFMEA as financial advisor.

In response to a question from Chairman Damron, Mr. Howard said last year the state sold approximately \$200 million in TRANS at the beginning of the year. He said that was the only TRAN issued for last year, but since all moneys from the Budget Surplus this year are already committed to projects included in the Surplus Expenditure Plan, there may be an opportunity to increase this year's TRAN size by issuing an additional TRAN at a later date. (Federal IRS rules limit the size of TRANS to anticipated cash flow shortages.) Mr. Howard said the sizing of last year's TRAN was as close to optimal as possible.

Chairman Damron asked what would happen if the state oversized its TRAN issue and issued bonds in excess of actual cash flow shortages. Mr. Howard responded the state would owe any of the excess earnings and some interest to the IRS, but there would be no penalty. He said the problem with issuing TRANS is the rules require the issuer to be able to anticipate deficits in advance.

Senator Buford made a motion to approve the KALC General Fund Tax and Revenue Anticipation Notes, 1998 Series A. The motion was seconded by Representative Wayne and passed by voice vote.

Chairman Damron asked Senator Leeper to take over duties of the Chair for the next two agenda items. Senator Leeper called on Mr. Howard to report on six new SFCC issues, two which required a tax increase: Daviess Co. - \$5,290,000 to refund

Representative Marcotte made a motion to approve the school bond issues with SFCC participation in debt service. The motion was seconded by Representative Wayne and passed by voice vote. Chairman Damron abstained from the vote, citing a possible conflict of interest.

Senator Leeper said there were two proposed tax and revenue anticipation notes to be 100% locally-funded: \$30,000,000 for the Jefferson County Board of Education and \$100,000,000 for the Kentucky Interlocal School Transportation Association on behalf of approximately 85 school districts. Proceeds from both bond issues will be used to meet cash flow shortages. Also, two other local school bond issues, which do not require a tax increase, were reported: Madison Co. - \$5,000,000 to complete additions and renovations to an elementary school; and Warren Co. - \$1,665,000 for HVAC renovations at two elementary schools.

Senator Leeper said no action was required on school bond issues that are 100% locally-funded.

Chairman Damron said the updated monthly/weekly debt issuance calendar was enclosed in members' folders, along with two information items: correspondence from the Governor's Office for Policy and Management regarding capital project administration and a listing of 1998-2000 projects authorized by the 1998 General Assembly.

Chairman Damron said the next meeting is scheduled for July 21, 1998, at 1:00 p.m. in Room 129 of the Capitol Annex.

With there being no further business, the meeting was adjourned at 2:30 p.m.